BEFORE

THE PUBLIC SERVICE COMMISSION OF

SOUTH CAROLINA

DOCKET NO. 97-131-W - ORDER NO. 1999-281

APRIL 20, 1999

IN RE: Application of Sigfield Water Company for Approval of an Increase in its Rates and Charges for Water Service.	)))	ORDER APPROVING RATES AND CHARGES

This matter comes before the Public Service Commission of South Carolina (the Commission) on the Application of Sigfield Water Company, Inc. (Sigfield or the Company) for approval of a new schedule of rates and charges for water services provided to its customers in Clarendon County, South Carolina. The Company's October 21, 1998 Application was filed pursuant to S.C. Code Ann. Section 58-5-240 (Supp., 1998), as amended, and 26 S.C. Regs. 103-821 (1976), as amended.

By letter, the Commission's Executive Director instructed the Company to publish a prepared Notice of Filing, one time, in a newspaper of general circulation in the area affected by the Company's Application. The Notice of Filing indicated the nature of the Company's Application and advised all interested parties of the manner and time in which to file appropriate pleadings. Additionally, the Company was instructed to directly notify all of its customers affected by the proposed increase. The Company submitted affidavits indicating that it had complied with these instructions. A Petition to Intervene Out-of-Time filed by the Consumer Advocate for the State of South Carolina (the Consumer Advocate) was granted.

The Commission Staff made on-site investigations of the Company's water system, audited the Company's books and records, and gathered other detailed information concerning the Company's operation.

On March 11, 1999, a public hearing concerning the matters asserted in the Company's Application was held in the Commission's Hearing Room at 101 Executive Center Drive, Columbia, South Carolina. Pursuant to S.C. Code Ann. Section 58-3-95 (Supp. 1998), a panel of three Commissioners, composed of Commissioners Bradley, Clyburn, and Moseley was designated to hear and rule on this matter. Chairman Bradley presided.

Sigfield was represented by William F. Austin, Esquire, and John J. Fantry, Jr., Esquire. Sigfield presented the testimony of Harold A. Sigmon and Penny L. Scheele. The Consumer Advocate was represented by Elliott F. Elam, Jr., Esquire, and Charles M. Knight, Esquire. The Consumer Advocate presented no witnesses. The Commission Staff (the Staff) was represented by F. David Butler, General Counsel. The Staff presented the testimony of Steve W. Gunter, Accountant/Fiscal Analyst, and Charles A. Creech, Associate Engineer. Members of the public were also heard by the Commission.

Upon full consideration of the Company's Application, the evidence presented at the hearing, and the applicable law, the Commission makes the following findings of fact and conclusions of law:

FINDINGS OF FACT

1. Sigfield Water Company is a water utility operating in Clarendon County, South Carolina, and is subject to the jurisdiction of the Commission pursuant to S.C. Code Ann. Section 58-5-10 (1976) et seq.

2. The Company operates a water system in the Lake View Subdivision which provides service to 70 residential customers and 3 commercial customers.

3. Sigfield's present water rates and charges were approved by Order No. 93-887, filed under Docket No. 91-155-W, dated October 1, 1993.

4. The Company's present unmetered residential rates are an annual fee of $320.04 or a flat rate of $26.67 per month. The present tap fee is $500.00.

5. Sigfield proposes to increase its rates as follows: Residential-Annual charge per single residence or single family equivalent: $510.00. Commercial rates would consist of a $996.00 annual charge for a ¾ inch tap, and a $1,476.00 annual charge for a 1 inch tap. The Company also proposes a Commodity Charge as follows: the first 2,000 gallons for the monthly minimum charge; 2,000 to 5,000 gallons at $3.75 per thousand gallons; 5,000 gallons and over at $3.50 per thousand gallons. In addition, Sigfield proposes to continue the one-time residential tap fee of $500.00. The Company also proposes a one-time commercial tap fee of $1,000 for a ¾ inch tap, and $1,250.00 for a 1 inch tap.

6. The appropriate test period for the purposes of this proceeding is the twelve-month period ending December 31, 1997.

7. Harold Sigmon, Company President, testified, as did Penny L. Scheele, an accountant. Both stated that the present rate does not allow the Company to meet its

operating expenses and costs. Company testimony was that, for the test year, the Company's income was $23,443.00 and expenses were $38,757.00, which resulted in a net loss of $15,314.00. According to Scheele, the Company is being subsidized by Mr. Sigmon. Further, Sigmon notes that the Safe Drinking Water Act has mandated changes and will increase system costs by $4,000. Also, property taxes have been increased by $521.00. On per-book basis, Staff found a Net Loss for Return of ($6,596). After accounting and pro forma adjustments, Staff found a Net Income for Return of $4,747.

8. Sigmon testified as to the fact that the largest users of water on the system are the Company's commercial customers. Sigmon states a belief that the commercial accounts are not supporting the system expense in proportion to their use. The commercial rates proposed by Sigfield attempt to address this concern.

9. Under the Company's presently approved rates, the Company's operating revenues for the test year after accounting and pro forma adjustments are $23,363. The Company seeks an increase in its rates and charges for water services in a manner that would increase its operating revenues by $20,444 to $43,807. See Hearing Exhibit 3, Accounting Exhibit A.

10. The Company's total operating expenses, under its presently approved rates, for the test year, after accounting and pro forma adjustments is $18,648.

11. The Commission will use the operating margin as a guide in determining the lawfulness of the Company's proposed rates and the fixing of just and reasonable rates.

12. A fair operating margin that the Company should have the opportunity to earn is 27.91%, which is produced by the appropriate level of revenues and expenses found reasonable and approved herein.

13. The rate designs and rate schedules approved by the Commission as described herein are appropriate and should be adopted.

14. The rates and charges depicted in Appendix A, attached herein, and incorporated by reference, are approved and effective for service rendered on or after the date of this Order.

DISCUSSION AND CONCLUSIONS OF LAW

1. The Company is a water utility providing water service in its service area in South Carolina. The Company's operations in South Carolina are subject to the jurisdiction of the Commission pursuant to S.C. Code Ann. Section 58-5-10 et seq. (1976) as amended.

2. A fundamental principle of the ratemaking process is the establishment of an historical test year with the basis for calculating a utility's rate base and, consequently, the validity of the utility's requested rate increase. While the Commission considers a utility's proposed rate increase based upon occurrences within the test year, the Commission will also consider adjustments for any known and measurable out-of-test year charges and expenses, revenues, and investments, and will also consider adjustments for any unusual situations which occurred in the test year. See Southern Bell Telephone & Telegraph Company v. The Public Service Commission of South Carolina, 270 S.C. 590, 244 S.E. 2d 278 (1978).

3. The Company chose the test year ending December 31, 1997. The Commission Staff used the same test year in calculating its adjustments. The Commission is of the opinion that the test year ending December 31, 1997 is appropriate for the purposes of this rate request, based on the information available to the Commission.

4. The Commission Staff proposed a number of accounting and pro forma adjustments to the Company's per book figures. Staff proposed to correct two errors found during the audit, the first adjustment being for revenues and the second for operating and maintenance (O&M) expenses. Staff's adjustment to operating revenues was ($80), and O&M was adjusted by $318, respectively. We approve these corrective Staff adjustments. Staff also adjusted non-allowable items and items which should have been capitalized by adjusting O&M expenses by ($1,633). We hold that this adjustment is also a proper one, upon examination of the record.

The most controversial Company adjustment in the case was a proposed allowance of $12,000 for a management agreement between the Company and Harold A. Sigmon, Sr. and/or Sumter Reforestation, Inc. (Sumter). Under the agreement, Sigmon and/or Sumter Reforestation, Inc. provided various management services to the Company. Staff proposes a disallowance of $9,600.

The difficulty is that this agreement has never been approved by this Commission, pursuant to the requirements of our Regulation 103-743. This would be a good enough reason, in our opinion, to disallow the entire agreement, which we did in the Company's last rate case. However, the Staff audit shows the provision of some services to the utility. Therefore, Staff concluded that a partial allowance for the management contract was appropriate. This was the same level of allowance approved by the Commission in the

Company's rate increase request in Docket No. 88-68-W. Reluctantly, we adopt the Staff's adjustment, since some evidence of the provision of services was found during the Staff's audit.

Both Company and Staff proposes to decrease expenses for non-recurring appraisal fees. Staff proposes to annualize depreciation expense using currently approved depreciation rates and year end plant in service. An adjustment of ($2,631) is recommended. In addition, Staff proposes to annualize depreciation expense for a personal computer that was purchased after the end of the test year, and used by both the Company and Sumter Reforestation. Staff allocated 50% of the cost of the computer to the utility. We believe that both of these adjustments are appropriate. We believe that the depreciation adjustment is correctly based on currently approved depreciation rates and year end plant in service, and the computer adjustment is appropriate, since both the Company and Sumter Reforestation used it.

The Company proposed to increase depreciation expense for the estimated cost of complying with a Department of Health and Environmental Control (DHEC) upgrade. Staff did not believe the adjustment was appropriate, because of the fact that the proposed adjustment was an estimate. We agree with the Staff, and reject the adjustment on the basis of it being an estimate.

A five year amortization period was proposed by the Company for rate case expenses, versus a three year period proposed by the Staff. We believe the Staff's proposed period represents a more reasonable period in which to recover the expenses.

Both the Staff and the Company propose to adjust property taxes. Staff's adjustment was based on invoices from Clarendon County for the year ended December

31, 1997, received and paid in 1998. According to Staff, the Company erred in its calculation of property tax, and Staff corrected this error in its adjustment. Based on this information, we adopt Staff's adjustment.

Adjustments to DHEC testing amounts were declined by Staff, due to the fact that only an estimate was available at the time of the audit. However, we have further examined the record in this case, and find that DHEC testing expense was included in cost of service during the year, and recovered through a pass through from the customers. Accordingly, the $1,346 expense by the Company during the test year is hereby eliminated for ratemaking purposes.

The Commission Staff proposed that interest expense for operating margin be reduced from the Company's requested $8,718 to $2,042, based on the Commission's standard formula for permissible interest. We hold that the standard formula is appropriate for this case, and the Staff's adjustment is correct. The premise of the formula is to allow interest only on long term debt used to construct plant, i.e. net plant. The formula therefore subtracts donated plant and accumulated depreciation from per books plant in service, including plant additions and cash working capital. To this figure, we apply the debt ratio and embedded rate of interest. In this case, $2,042 is the interest allowable on the net plant service and/or the interest on the long term debt used to construct the plant. The Company requested interest on all of plant in service. It was only entitled to interest on net plant in service.

Staff proposes to adjust income taxes using current Federal and State income tax rates. Staff's adjustment also included the effects of synchronized interest. The question that evolved during the hearing, as per cross-examination by the Consumer Advocate, had to do with the fact that the Company is a Subchapter S corporation, which under these particular circumstances, encountered no tax liability. The Staff's adjustment was based on the fact that tax liability was generated for individual shareholders of the Company. We approve the Staff's adjustment. In this situation, tax liability is generated for the Company's shareholders, who are then responsible for any tax liability. Since a tax liability is generated, we believe it is appropriate to allow an income tax adjustment, such as that made by Staff in this case, since taxes must eventually be paid by the true owners of the Company, the shareholders.

5. The Commission concludes that after pro forma and accounting adjustments, the Company's test year operating revenues, operating expenses, and net income for return for its system were $23,363, $18,648, and $4,748. These figures are reflected in Table A as follows:

TABLE A

NET INCOME FOR RETURN

BEFORE RATE INCREASE	
Operating Revenues	$23,363
Operating Expenses	18,648
Net Operating Income	4,715
Customer Growth	33
Total Income for Return	$ 4,748

6. Under the guidelines established in the decisions of Bluefield Water Works and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923), and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591

(1944), this Commission does not ensure through regulation that a utility will produce net revenues. As the United States Supreme Court noted in Hope, a utility "has no constitutional rights to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures." However, employing fair and enlightened judgment and giving consideration to all relevant facts, the Commission should establish rates which will produce revenues "sufficient to assure confidence in the financial soundness of the utility...that are adequate under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties." Bluefield, supra, at 692-693.

7. There is no statutory authority prescribing the method which this Commission must utilize to determine the lawfulness of the rate of a public utility. For a water utility whose rate base has been substantially reduced by customer donations, tap fees, contributions in aid of construction, and book value in excess of investment, the Commission may decide to use the "operating ratio" or "operating margin" method for determining just and reasonable rates. The operating ratio is the percentage obtained by dividing total operating expenses by operating revenues; the operating margin is determined by dividing the total operating income for return by the total operating revenues of the utility.

8. The Commission concludes that the use of the operating margin is appropriate in this case. Based on the Company's gross revenues, operating expenses, and customer growth for the test year, the Company's present operating margin for combined operations is as follows:

TABLE B

OPERATING MARGIN

BEFORE RATE INCREASE

Operating Revenues	$23,363
Operating Expenses	18,648
Net Operating Income	4,715
Customer Growth	33
Total Income for Return	$ 4,748
Operating Margin	11.58 %
Interest Expense for Operating Margin	$ 2,042

9. The Commission is mindful of the standard delineated in the Bluefield decision and of the need to balance the respective interests of the Company and of the consumer. It is incumbent upon this Commission to consider not only the revenue requirement of the Company but also the proposed price for the water treatment, the quality of the water service, and the effect of the proposed rates upon the consumers. See Seabrook Island Property Owners Association v. South Carolina Public Service Commission, 401 S.E. 2d 672 (1991); S.C. Code Ann. Section 58-5-290 (1976) as amended.

10. Based on the considerations enunciated in Bluefield and Seabrook Island, the Commission determines that the Company should have the opportunity to earn $7,147 in additional operating revenues, for a total of $30,510 in operating revenues. Taking into consideration Total Operating Expenses of $20,024, Net Operating Income of $10, 486, Customer Growth of $72, a Net Income for Return of $10,558, and Interest Expense of

$2,042, the Commission determines that the Company should have the opportunity to earn a 27.91% operating margin. This operating margin is within the range of operating margins allowed by this Commission for various water and wastewater cases heard by us between 1991 and 1998. (See chart submitted as part of Hearing Exhibit 4.) The numbers mentioned herein are illustrated by the table below:

TABLE C

OPERATING MARGIN

AFTER RATE INCREASE	
Operating Revenues	$30,510
Operating Expenses	20,024
Net Operating Income	10,486
Customer Growth	72
Total Income for Return	$10,558
Operating Margin	27.91%
Interest Expense for Operating Margin	2,042

11. The fundamental criteria of a sound rate structure have been characterized as follows:

> ...(a) the revenue-requirement or financial-need objective, which takes the form of a fair-return standard with respect to private utility companies; (b) the fair-cost apportionment objective which invokes the principle that the burden of meeting total revenue requirements must be distributed fairly among the beneficiaries of the service; and (c) the optimum-use or consumer rationing under which the rates are designed to discourage the wasteful use of public utility services while promoting all use that is economically justified in view of the relationships between costs incurred and benefits received.
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> Bonbright, Principles of Public Utility Rates (1961), p. 292.

12. In fashioning rates to give the Company the required amount of operating revenues so that it will have the opportunity to achieve an 27.91% operating margin, the Commission has carefully considered the concerns of the Company's customers as well as the interests of the utility. As stated above, Company President Sigmon testified that the largest users of water on the system were the commercial customers, and that these customers were not supporting the system expense in proportion to their use. The Company therefore proposed new commercial rates which would address these concerns. Accordingly, we hereby approve the proposed rate schedule for the commercial customers as filed, with the exception of the new proposed tap fees. We believe that these new rates require the commercial customers to carry more of their fair share of the system's expenses. We deny the new proposed commercial tap fees, however. A tap fee is defined as the cost of installing the utility's service line from the main to the customer's premises and a portion of plant capacity which will be used to proved service to the new customer. See Regulation 103-702.14. The Company simply did not justify the commercial tap fee requested. Sigmon's testimony showed the cost of a ¾ inch tap as $468.00 and a 1 inch tap as $581.00. No attempt was made to quantify the plant capacity portion of the tap fee. Accordingly, the proposed commercial tap fees are denied.

With further regard to the commercial rates, we hold that the commercial customers shall continue to pay $26.67 per month for water service until the expiration of a 30-day written notice period that the Company shall provide after installation of the meters. At the end of the 30-day notice period after meter installation, the Company may begin to charge the commercial metered rates approved herein.

Likewise, we do not think that the Company justified any increase in its residential rates. We would point out that the Company was earning an operating margin of 11.58% in this case after accounting and pro forma adjustments, and before the increase (including removal of DHEC testing fees). (Even Staff's original as adjusted figures, which did not remove DHEC testing fees from cost of service showed that the Company was earning a 6.90 % operating margin.) Although the Company showed some increase in expenses, it did not show enough of an increase to merit an increase in its residential rates, which shall remain the same. (The residential tap fee will also remain the same.) The Commission hereby approves the rates and charges as stated in this Order and attached hereto as Appendix A as being just and reasonable.

13. Accordingly, it is ordered that the rates and charges attached hereto as Appendix A are hereby approved for service rendered on or after the date of this Order. The rate schedule is hereby deemed to be filed with the Commission pursuant to S.C. Code Ann. Section 58-5-240 (Supp. 1998).

14. It is ordered that if the approved schedule is not placed in effect within three months after the date of this Order, the approved schedule shall not be charged without written permission of the Commission.

15. It is further ordered that the Company maintain its books and records for water operations in accordance with the NARUC Uniform System of Accounts for water and sewer utilities as adopted by this Commission.

16. This Order shall remain in full force and effect until further Order of the Commission.

BY ORDER OF THE COMMISSION:

Philip T. Bradley
Chairman

ATTEST:

Executive Director

(SEAL)

APPENDIX A

SIGFIELD WATER COMPANY, INC.
2911 WAVERLY DRIVE
SUMTER, SC 29150
(803) 481-3504

DOCKET NO. 97-131-W
ORDER NO. 1999-281
DATE: 4/20/99

COMMISSION GRANTS CUSTOMER THE OPTION OF PAYING ANNUALLY OR MONTHLY.

WATER SERVICE

Residential

Annual Service Charge – Flat Rate	$320.04
Or	
Monthly Service Charge – Flat Rate	$ 26.67

SCHEDULE OF OTHER CHARGES

Residential & Commercial

Tap Fee	$500.00

Commercial Monthly Rates

¾" Tap	
1st 2000 gallons	$ 83.00
2m to 5m gallons	$ 3.75/m
All over 5m gallons	$ 3.50/m
1" Tap	
1st 2000 gallons	$123.00
2m to 5m gallons	$ 3.75/m
All over 5m gallons	$ 3.50/m